CITIZENS PROPERTY INSURANCE CORPORATION AS “STRONG AND PROFITABLE”?

lYou may have read about Florida’s property insurance troubles and wondered where to turn for stability. Some recent reports have described Citizens Property Insurance Corporation, our government-run property insurer, as the “strongest and most profitable” insurer in the state. In fact, though Citizens is a needed consumer safety net, it is no substitute for a vibrant private market with diverse insurance options for Florida homeowners. A deeper look reveals the shaky assumptions behind some of its stated claims-paying capacity and highlights the immediate need for insurance law reforms that will benefit all Floridians, whether insured by Citizens or not. The right actions now will signal insurers around the globe to commit new capital to support Florida’s storm exposure – which represents 60% of all hurricane risk in the U.S. – and ultimately drive down rates while opening more insurance choices in all parts of the state.

Citizens is “profitable” only because hurricanes have not struck in five seasons – a historically lucky streak according to scientists. It looked pretty profitable before the 2004-2005 storms, too, and all Floridians paid for that illusion with a taxpayer bailout of $715 million in 2006, plus over $6 billion in assessments on most of your insurance policies from Citizens and its backup fund, the Florida Hurricane Catastrophe Fund. Citizens insures mostly coastal buildings and collects most of its premium for wind risk, but doesn’t pay it out absent a hurricane. In the next unlucky season, it will be on the hook for far more than its reserves, and could pay out $22 billion or more. “Profit” as an annual concept is meaningless when the risk is catastrophic hurricanes at unpredictable times.

These reports also assert that Citizens’ current “surplus” claims-paying capacity of over $5 billion is twice that of the combined private market insurers. But unlike Citizens, private insurers fund most of their hurricane risk each year by buying reinsurance (backup contracts) from investors such as Warren Buffett. In fact, if they didn’t, Florida’s insurance regulators would shut them down. Private insurer reserves are only needed to cover a small retained portion of the risk.

Citizens could use its surplus – but doesn’t – to “buy out” much of its risk this way. Instead, it and state leaders make the conscious choice to borrow billions from Floridians. Citizens sells bonds to Wall Street after storms and pays them off with those assessments. A big storm could result in a bill of hundreds or thousands of dollars for every family, business, and even charitable organization in the state, continuing for up to 30 years.

But as the reports state, at least Citizens can “guarantee” claim payment, right? Not so fast. Citizens relies on the Cat Fund more than any private insurer, using about 40% of the fund’s total capacity. The Cat Fund’s own chief notes this fund is not real reinsurance, just a trust fund obligated by law to pay only what it can, and its own promises exceed its reserves by $14 billion or more. The Cat Fund and Citizens together would beg stressed financial markets for tens of billions after a big storm, and if there is not enough appetite, claims don’t get paid – it’s that simple. Private insurers don’t have to rely on Wall Street – their reinsurers either fully collateralize their contracts, or have the highest financial strength ratings, and quickly cut checks.

Finally, suppose everything goes as planned after the storm for Citizens. What then? Florida would be billions deeper in debt, massive assessments would damage future economic growth, and Citizens’ coffers would be empty. Hopefully, our private insurers who for years competed with Citizens’ artificially low rates, responsibly funded and spread their risk around the world, promptly paid their storm claims, and renewed most of their policies would help us out.

By all means, let’s debate the role of the safety net in Florida property insurance, but use the same yardstick for both the private and public sector players. Only then can we find the clarity needed to determine what and where Citizens should insure, how much it should charge, and how it should ensure it can keep its promises.

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